Interlocutory Injunctions in the Franchise Context: Recent Trends

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INTRODUCTION

Injunctions play a key role in franchising. They enable franchisors to enforce in-term and post-term covenants contained in their franchising agreements to protect their brand, reputation and franchise system generally. They also allow franchisees to enjoin franchisors from wrongfully terminating their franchise relationship pending trial.

Where a franchisor seeks to enjoin a franchisee from breach of a restrictive covenant or a franchisee seeks to enjoin a franchisor from wrongfully terminating their relationship at an interlocutory stage, courts have generally followed a well-established formula or three-part test (the "Three-part Test"[2]). First, is there a serious issue to be tried? Secondly, will the moving party sufferable irreparable harm if the injunction is not granted? Finally, does the balance of convenience lie in favour of granting the injunction?

Although interlocutory injunctions to enjoin a breach of a negative covenant or termination of a franchise relationship are not granted automatically[3], and non-competition covenants are never presumed to be enforceable, where the facts of the case satisfy the Three-part Test, courts have typically granted an interlocutory injunction without applying a great deal of scrutiny to the case's merits.

Recent trends, however, indicate that there is some judicial debate regarding how to approach and apply the Three-part Test. In particular, there is a dichotomy as to whether the first part of the Three-part Test should be "serious issue to be tried" or the more stringent requirement of "strong *prima facie* case". In addition, where a franchisor seeks to enjoin a franchisee from breach of a non-competition covenant, courts are now requiring more concrete evidence of irreparable harm, rather than merely accepting that such breaches generally harm the franchise

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[2] The quintessential three-part test for an interlocutory injunction is set out in *R.J.R MacDonald Inc. v. Canada* (A.G.), [1994] 1 S.C.R. 31 at pp. 334 – 343.

[3] Justice Robert J. Sharpe, *Injunctions and Specific Performance*, 2nd ed., looseleaf (Aurora: Canada Law Book, 1992 -).

system. Thirdly, even where there is a clear breach of a restrictive covenant by a franchisee, courts increasingly require plaintiff franchisors to satisfy all three elements of the Three-part Test as opposed to only the first part of the Three-part Test. Indeed, Ontario courts appear to be looking more closely at the merits of a case at the interlocutory stage, and, as a result, it appears to becoming more difficult for franchisors to obtain an interlocutory injunction in Ontario courts. On the other hand, where franchisees seek to enjoin a franchisor from terminating a franchise agreement, courts continue to apply the lower threshold test and do not appear to apply the same degree of scrutiny.

FIRST TREND: THE THRESHOLD: FROM 'SERIOUS ISSUE TO BE TRIED' TO 'STRONG *PRIMA FACIE* CASE'

Traditionally, under the first part of the Three-part Test, courts have applied the threshold of "serious issue to be tried" in determining whether to grant an interlocutory injunction to enforce a restrictive covenant contained in a franchise agreement, such as a non-competition covenant. Indeed, the "serious issue" threshold has been applied by courts in the majority of franchise cases since the Three-part Test was articulated by the Supreme Court of Canada in *R.J.R. MacDonald Inc. v. Canada* ("*R.J.R. MacDonald*").[4] The "serious issue" threshold has generally been considered to be a relatively low one to meet and requires the judge hearing the injunction to be satisfied, based only on a preliminary assessment of the merits of the case, that the proceeding is neither frivolous nor vexatious. If there is a serious issue to be tried, then the judge proceeds to consider the other parts of the test, namely, irreparable harm and balance of convenience. As the Supreme Court of Canada stated in *R.J.R MacDonald*, this is so even if the judge is of the opinion that the franchisor is unlikely to succeed at trial. Accordingly, when applying the "serious issue" threshold, courts have typically not delved into the ultimate enforceability of either restrictive covenants in particular or franchise agreements in general, leaving more careful and detailed scrutiny of the merits of the case as a matter for the trial judge.[5]

However, recent developments suggest that where the enforcement of restrictive covenants is concerned, courts may be moving away from the relatively lower "serious issue" threshold, in favour of applying a more stringent test of "strong *prima facie* case".[6] To meet this threshold, a party seeking an interlocutory injunction must establish that "it is clearly right and that there is a high degree of assurance" of success of obtaining a permanent injunction at trial.[7] When

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[4] See for example *674834 Ontario Ltd. (c.o.b. Coffee Delight) v. Culligan of Canada Ltd.* (2007), 28 B.L.R. (4^{th}) 281 (Ont. Sup. Ct.) [*Culligan*] (a decision in which the authors' firm was counsel for the franchisor); *Allegra of North America Inc. v. Wayne Zapfe et al,* unreported (2001) (Ont. Sup. Ct.), leave to appeal denied, *Allegra of North America Inc. v. Zapfe* [2001] O.J. No. 5412 (Ont. Sup. Ct.) [*Allegra I*]; *Ontario Duct Cleaning v. Wiles et al,* [2001] O.J. No. 5150 (Ont. Sup. Ct.) [*Ontario Duct Cleaning*], (a decision in which the authors' firm was counsel for the franchisor); and *CashMoney Express Inc. v. 1035216 Ontario Inc.,* unreported (2003) (Ont. Sup. Ct.) [*CashMoney*].

[5] See for example, *Allegra I, Ontario Duct Cleaning* and *CashMoney, supra* note 4. In granting the injunctions in these cases, the court found that there was at least a serious issue to be tried as to the clauses' enforceability.

[6] This higher threshold of strong *prima facie* case has typically been applied to the enforcement of restrictive covenants in the employment context, where enjoining an individual would have severe consequences of loss of livelihood and chosen vocation. See comments of Justice Nordheimer in *Jet Print Inc v. Cohen*, [1999] O.J. No. 2864 (Ont. Sup. Ct.).

[7] *Culligan, supra* note 4 at para. 26.

applying this standard, the court will carefully examine the text and context of the franchise agreement and consider the enforceability of particular covenants within the agreement.[8] Closer scrutiny of the *ultimate enforceability* of the non-competition covenant(s) at issue appears therefore to be a key feature of this recent movement towards the more rigorous "strong *prima facie* test" standard.

For example, in *Second Cup Ltd. v. Niranjan* ("*Second Cup*")[9], the court scrutinized the post-termination non-competition clause contained in a franchise agreement which had only been signed by the franchisee in spite of the franchisor having expressly required execution of all documents by all of the parties. The court found that the non-competition clause was unenforceable on the basis that there was "nothing in the conduct of the parties which would suggest that they clearly assented to the precise terms of section 12 [the non-competition clause] of the franchise agreement"[10]. Although the franchisee admitted that some obligations were owed to the franchisor upon termination, she was unclear as to the precise terms. As a result, the court stated that "…the evidence is not sufficient to show that parties are bound by the non-competition covenant, and, accordingly, Second Cup has not made out a strong *prima facie* case"[11].

Why strong *prima facie* case and not a serious issue to be tried standard? Justice Lederman explained that some circumstances "call for a stricter standard".[12] In *Second Cup*, the circumstances were that the granting of an interlocutory injunction would lead to the final determination of the issues at hand as the 15-month non-competition period would, in the court's view, be completed before the trial would ever take place.[13] In addition, His Honour relied on the fact that the franchisor was seeking to enforce a restrictive covenant.[14] For this proposition,

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[8] See *Lombardo v. Ragno*, [2001] O.J. No. 1300 (Ont. Sup. Ct.) [*Lombardo*] and *Second Cup Ltd. v. Niranjan*, 2007 CarswellOnt 5285 (Ont. Sup. Ct. [Commercial]) [*Second Cup*] (a decision in which the authors' firm was counsel for the franchisor).

[9] *Second Cup*, *supra* note 8.

[10] *Ibid*. at para. 19.

[11] *Ibid.* at paras. 26-27.

[12] *Ibid*. at para. 22.

[13] Presumably the court could have ordered an expedited trial like it did in the *Hyundai* case, at note 19, *infra*. In *Second Cup*, the franchise agreement expired on May 30, 2007 and the non-competition covenant was for fifteen months. There was ample time for a trial to be scheduled prior to the expiry of the non-competition covenant, especially since the matter was on the Commercial List.

[14] See franchise cases referred to in note 4, *supra*, where a non-competition covenant was enforced and only the serious issue standard was applied. Even though the injunction was denied in *Allegra II*, the court applied the serious issue standard. See also *W.A.B. Bakery Franchising Ltd. v. Canam Advertising Ltd. and Raphi Shram*, (2007) CarswellOnt 8989 (Ont. Sup. Ct.) [*W.A.B. Bakery*], at note *28*, *infra*. *1460904 Ontario Inc. v. MDG Computers Canada Inc.*, [2006] CarswellOnt 6744 (Ont. Sup. Ct.) [*MDG Computers*] is another example of a franchisor being held to the strong *prima facie* case standard. However, the primary focus in that case was on the franchisor's request for a mandatory injunction requiring the franchisee to assign a lease, as opposed to the franchisor's request to compel the franchisee to comply with a post-termination non-competition covenant. The authors are not aware of any other franchise case in which a franchisor seeking to enforce a non-competition covenant was held to the *strong prima facie* standard. *Second Cup*, therefore, appears to be an anomaly.

the court referred to *Lombardo v. Ragno* ("*Lombardo*")[15], a 2001 decision of the Ontario Superior Court of Justice. Importantly, *Lombardo* was not a franchise matter, but rather involved a non-competition covenant contained in a shareholder agreement. In *Lombardo*, the court took issue with the plaintiff's interpretation of the non-competition clause. Specifically, the court found that the plaintiffs were "seeking to enforce a negative obligation that would severely and substantially impair the rights of the defendants to make their living".[16] The court determined that in circumstances where the rights of a party to make their living in their business would be substantially impaired by granting an interlocutory injunction, the "more stringent aspect of strong *prima facie* case is apt".[17]

Whether the "serious issue to be tried" or "strong *prima facie* case" threshold is applied by the court appears also to largely be influenced by the practical effect of enforcing the covenant at issue. Where enforcing a restrictive covenant will impose an obligation on a party to act positively, it is viewed as a mandatory injunction and the plaintiff will have to meet the higher threshold of demonstrating that it has a strong *prima facie* case.[18] On the other hand, courts are more inclined to apply the serious issue to be tried threshold where enforcing a restrictive covenant does not substantially alter the *status quo*, and does not create an obligation, but rather holds parties to their existing obligations. Therefore, franchisors arguably will have greater success with meeting the first threshold of the Three-part Test if they can demonstrate the express terms of the restrictive covenant, and specifically that it relates to an *existing* or *on-going obligation*, rather than creating a new obligation. Based on this distinction, had the franchise agreement in *Second Cup* been signed by both parties, then there would have been grounds for the Court to apply the serious issue standard.

Conversely, where a franchisee seeks to enjoin a franchisor from wrongfully terminating a franchise agreement pending trial, courts appear to be more inclined to apply the lower threshold of "serious issue to be tried". In *Culligan*, for example, the court held that there was an existing agreement between the parties (even though it had been terminated by Culligan on notice and the distributor had only come to court after the effective termination date), and the plaintiff distributor was therefore seeking to continue its rights under that agreement until trial. Finding that the plaintiff distributor's case was not frivolous or vexatious, and characterizing the injunction as prohibitive, the court applied the serious issue threshold.

Ontario Ltd. v. Hyundai ("*Hyundai*")[19] is a more recent example of an attempt by a franchisee to enjoin a franchisor from terminating the dealer agreement between the parties. In *Hyundai*, the court considered the appropriate test to be applied on an interlocutory injunction motion. The franchisor, like the franchisor in *Culligan*, argued that the franchisee's case should be measured against the higher standard of strong *prima facie* case because the relief sought by the franchisee dealer was mandatory, rather than prohibitive in nature as it would require the franchisor to allow

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[15] *Lombardo*, *supra* note 8.

[16] *Ibid.* at para. 16.

[17] *Ibid*.

[18] See for example *Culligan*, *supra* note 4, and *MDG Computers*, *supra* note 14.

[19] *1323257 Ontario Ltd. (c.o.b. Hyundai of Thornhill) v. Hyundai Auto Canada Corp.*, [2009] O.J. No. 95 (Ont. Sup. Ct.).

a terminated dealer agreement to continue. The court considered previous cases where courts had examined whether the dealership agreement contained renewal rights as a factor in determining whether an injunction would be prohibitive or mandatory, and the appropriate standard to be applied. The court noted that in cases where a right of renewal exists, requests for injunctive relief have typically been viewed as prohibitive because the plaintiff seeks to prevent the denial of a right already existing or agreed upon. On the other hand, where no renewal rights existed, injunctive relief was characterized as mandatory relief because it involved creation of a right or requiring the defendant to do something it had not previously contracted for or agreed to. The dealership agreement in *Hyundai* contained an annual automatic renewal clause. Accordingly, the court found that the applicable standard was serious issue to be tried, as the essence of the injunctive relief sought was to preserve until trial the *status quo* of the dealership relationship, rather than create a new obligation to be imposed on the defendant.

In *Struik v. Dixie Lee Food Systems Ltd.*,[20] Justice Whalen also considered the distinction between prohibitive and mandatory interlocutory remedies in the context of terminating a franchise agreement. The franchise agreement at issue did permit termination without prior notice where the franchisee fail[ed] "to actively and continuously operate the business…up to the standards and reasonable expectations of the Franchisee", and thirteen more years remained in the term of the franchise agreement.[21] Justice Whalen found that although the franchisee's case met the higher standard required for a mandatory interlocutory injunction, in the circumstances of the case, where the franchisee sought simply to continue the rights agreed to under the franchise agreement and maintain the *status quo*, the relief sought by the franchisee was not mandatory in nature.[22] Justice Whalen stated that "it is a question of prohibiting termination of pre-existing rights, rather than requiring Dixie to do or not do something it had not already agreed to".[23]

The analyses in *Second Cup*, *Hyundai*, *Culligan* and *Struik* suggest that Ontario courts may apply greater scrutiny to the merits of cases where a franchisor seeks to enjoin a franchisee from breach of a restrictive covenant than where a franchisee (/distributor) seeks to enjoin a franchisor from terminating an agreement pending trial. Indeed, while a franchisee need only demonstrate that his case is not frivolous or vexatious, a franchisor who wishes to enforce a restrictive covenant may have to show a high degree of assurance of success at trial. Interestingly, while courts are inclined to characterize enforcement of a restrictive covenant against a franchisee as a mandatory injunction, mandating the higher threshold, requiring a franchisor to continue a terminated

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[20] *Struik v. Dixie Lee Food Systems Ltd.*, [2006] O.J. No. 3269 (Ont. Sup. Ct.) [*Struik*]

[21] *Ibid.* at paras. 20 and 76.

[22] *Ibid.* at paras. 64 and 72.

[23] *Ibid.* at para. 72. See also *Erinwood Ford Sales Ltd. v. Ford Motor Co. of Canada*, [2005] O.J. No. 1970 (Ont. Sup. Ct.) [*Erinwood*], in which the court distinguished between mandatory and prohibitive injunctive relief. In *Erinwood*, Justice Spies wrote: "I agree with the observation of the Divisional Court in the TDL Group decision, that, distinguishing between positive and negative orders is not always clear-cut. It is somewhat like the old question of "is the glass half empty or half full?" Notwithstanding that it can be argued that there is a mandatory nature to the order sought by the plaintiffs, in that it requires the defendant to continue to comply with the terms of the Dealership Agreement, there is no question that granting the injunction creates no new rights. The plaintiffs seek to preserve the status quo pending trial and in my view, as a result, the order sought is not a mandatory injunction."

franchise agreement or relationship is not viewed as imposing a positive obligation. However, requiring a franchisor to continue such a relationship is arguably imposing a positive obligation upon it where that franchisor has a right to terminate the relationship under the franchise agreement.

Courts have held that "categories of positive and negative covenants and orders are not clear-cut" and that whether the particular relief sought is prohibitive or mandatory in nature is determined by its "factual matrix".[24] It appears, therefore, that franchisors may have greater success in obtaining injunctions to enforce a restrictive covenant if they are able to frame the injunction as prohibitive, in accordance with an unequivocal and existing agreement, rather than mandatory. Similarly, where a franchisee seeks to enjoin the termination of a franchise agreement, a franchisor challenging that injunction might have resort to the higher standard of strong *prima facie case* if continuance of the agreement can be persuasively characterized as imposition of a positive obligation upon the franchisor.

SECOND TREND: GREATER EVIDENTIARY BURDEN FOR DEMONSTRATING IRREPARABLE HARM

The movement towards a higher standard for assessing the strength of the plaintiff's case on an interlocutory injunction motion also appears to be coupled with more rigorous evidentiary requirements for demonstrating irreparable harm[25], the second element of the Three-part Test.

In the past, courts have accepted arguments from counsel that a franchisee or former franchisee's breach of a restrictive covenant causes damage to the franchise system generally, and therefore satisfies the second criteria of the Three-part Test: irreparable harm. In *Allegra of North America Inc. v. Wayne Zapfe et al* ("*Allegra I*"), the court found that damages alone would not be an adequate remedy, and emphasized the importance of maintaining the integrity of the franchise business. Specifically, the court stated that if franchisees are permitted to carry on a "shadow business", "the character of franchisor's business will be changed. It will be carrying on a training business, not a franchise business. The core of the franchise system will be destroyed."[26]

Courts have also traditionally considered breaches of restrictive covenants of franchisees to constitute irreparable harm because of the potential for such breaches to encourage other franchisees of that franchisor to learn from example and similarly breach a non-competition covenant.[27]

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[24] *TDL Group Ltd. v. 1060284 Ontario Ltd.*, [2001] O.J. No 3614 (Ont. Sup. Ct. [Divisional Court]) at para. 4; *Culligan*, *supra* note 4 at para. 33; *Erinwood*, *supra* note 23 at 72.

[25] Irreparable harm is defined as harm that cannot be readily compensated for in damages, and refers to the unquantifiable nature of the harm suffered, rather than its magnitude. *R.J.R. MacDonald Inc.*, *supra* note 2.

[26] *Allegra I*, *supra* note 4. See also *Ontario Duct Cleaning* and *CashMoney*, *supra* note 4, in which the court stated: "A decision to allow a person whose franchise agreement has been terminated to commence a similar business in a franchised area would have an impact on all franchise systems".

[27] See for example *CashMoney*, *supra* note 4: "If [the defendant] can continue to operate a similar business from the same premises or within the franchised area it could jeopardize the Canadian Franchise system because other Cashplan franchisees may do so the same as the defendant has done".

However, recent decisions suggest a growing reluctance of courts to accept principles of general harm to the franchise system, or arguments that breach by one (former) franchisee will encourage a domino effect of breaches by other franchisees, in the absence of actual evidence of such harm. Indeed, courts are increasingly requiring plaintiffs to meet a higher evidentiary burden of demonstrating specific examples of irreparable harm.

For example, in *W.A.B Bakery Franchising, supra*, the franchisor (What A Bagel) argued that the integrity of its franchise system would be undermined if a non-competition covenant were not enforced because the conduct of the former franchisee would encourage other franchisees to breach their own non-competition covenants when their franchise agreements expired. What A Bagel further argued that failure to enforce the non-competition covenant would result in the reluctance of prospective What A Bagel franchisees to enter into franchise agreements for new locations. Additionally, What A Bagel argued that it would suffer a loss of goodwill if the products served by the former franchisee in its new business did not meet the quality of products served at other What A Bagel franchises. The court agreed that What A Bagel would suffer irreparable harm if similar action were taken by other franchisees in the future, but rejected What A Bagel's arguments on account of its failure to provide evidence of such action being taken or threatened at the time of the application or in the future. Furthermore, there was no evidence of prospective franchisees deciding not to enter into franchise agreements for new locations as a result of the former franchisee's actions.

In *Second Cup, supra*, the court rejected the franchisor's argument that it would suffer irreparable harm if the franchisee was allowed to continue its newly established coffee operation, as this would send a message that Second Cup franchises can be used as a training ground to open up competing retail coffee enterprises, thus compromising the integrity of the Second Cup franchise system. The court found that there were significant differences between the business models of Second Cup and its former franchisee, specifically that the coffee and tea sold by the former franchisee's new café was fair trade and organically grown, while this was not the case at Second Cup cafés. The court held that because of this distinction between the two operations, there had not "been any significant adverse effect to the integrity of Second Cup's franchise system".[28] Further, any damages suffered by Second Cup in lost customers could be calculated as money damages.

In *Allegra of North America and Allegra Corporation of Canada v. Russell Sugimura et al ("Allegra II")*[29], the court rejected the franchisor's argument that irreparable harm would result from breach of a non-competition covenant because other franchisees would feel at liberty to disregard their non-competition covenants. In its decision, the court noted that Allegra's assertion of irreparable harm was "not based on any irreparable harm flowing from the breach of

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[28] *Second Cup*, *supra* note 8 at paras. 29-31.

[29] *Allegra of North America and Allegra Corporation of Canada v. Russell Sugimura et al.*, (2008) (unreported) Court File No. CV-08-21790-00 (Ont. Sup. Ct.) [*Allegra II*]. The case involved an application for an interlocutory injunction to restrain former franchisees from carrying on a printing business at the same location where an Allegra franchise was operated for many years. Allegra alleged that the former franchisees violated their post-expiration non-competition covenant because one of the former franchisees was employed by a new printing/copying business operating out of the same location as the former Allegra location. Dismissing the franchisor's application, the court held that the franchisor failed to demonstrate that irreparable harm would result from failure to grant injunctive relief.

the Franchise and License Agreement with the defendants", indicating that in order to demonstrate irreparable harm, a franchisor must give specific evidence of irreparable harm flowing from the breach at issue, rather than potential future harm. Importantly, the court in *Allegra II* found that in seeking to enjoin its former employee, the franchisor had no legitimate business interest to protect in the geographic area in which the former franchisee was employed (on account of there being no franchise in the area), and that there was no evidence that the franchisor intended to establish or maintain a franchise in that geographic area after the expiry of the franchise agreement. As a result, the court held that the non-competition covenant was unenforceable. To enforce it in the circumstances would serve no valid purpose as it was not reasonably required for the franchisor's protection.[30] Interestingly, in *Allegra II*, the court applied the lower "serious issue to be tried" threshold, and found that although there was a serious issue to be tried as to the *enforceability* of the non-competition covenant, the absence of any sustainable claim for damages or irreparable harm flowing from breach of the covenant meant that the threshold was not met. The decisions in *Allegra II*, *W.A.B. Bakery* and *Second Cup* are potentially critical as they place an elevated burden on franchisors to demonstrate irreparable harm that goes beyond general threats to the integrity of the franchise system or compromised goodwill. These cases suggest that when seeking an interlocutory injunction to enforce a post-termination restrictive covenant, a franchisor should be prepared to provide concrete evidence demonstrating it has a legitimate business interest to protect, in the form of an actual or planned franchise.

Conversely, it appears that courts will not apply the same scrutiny to evidence of irreparable harm adduced by franchisees. In *Culligan*, *supra*, the defendants took issue with the plaintiff distributor's statement that 90% of its sales were in respect of the defendant's bottled water, and that if it was unable to supply this water it would go out of business. These statements were not substantiated by evidence as to either volume of sales or lack of alternative suppliers of water. Although the court agreed that bald statements are not sufficient to establish irreparable harm, it did not scrutinize the plaintiff's statements. Rather, viewed in the context of the plaintiff being a small company, and its "significant reliance" on sales of the defendant's bottled water, the court did not find the plaintiff's assertions of irreparable harm to be "bald statements".[31]

In *Struik*, *supra*, the franchisor argued that the franchisee did not discharge his evidentiary burden in demonstrating irreparable harm.[32] Finding that the termination of the franchise agreement had indeed caused the franchisee to suffer irreparable harm, Justice Whalen observed that although the franchisee's age was not stated, he was "obviously a man of at least 60 years" and had "therefore devoted the better part of his working life to [the] franchise…the issue is the loss of long-established means to pursue a rewarding livelihood, not proving financial hardship or destitution".[33] Further, His Honour wrote that "although not much was made of [the franchisee's relationship with other franchisees] in argument, I am convinced there is probably a proprietary and goodwill aspect to JS's status as an area franchisee", and that quantification of

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[30] *Allegra II*, *supra* note 29 at para.22 29.

[31] *Culligan*, *supra* note 4 at paras. 42 and 43.

[32] *Struik*, *supra* note 20 at para 67.

[33] *Ibid.* at para. 73.

the proprietary aspects of JS's interest in the Area Franchise Agreement would be difficult.[34] *Struik* and *Culligan* arguably suggest that in the context of wrongful termination cases, franchisees seeking interlocutory relief may not face the same rigorous evidentiary hurdle faced by franchisors to demonstrate irreparable harm.

THIRD TREND: AFFIRMATION OF THE THREE-PART TEST

Courts have affirmed that irreparable harm and balance of convenience are factors which must be considered in determining an interlocutory injunction, even where there is unequivocal evidence of breach of a restrictive or negative covenant. Previous decisions such as *Ontario Duct Cleaning Ltd, supra*, *CashMoney, supra*, and *Button v. Jones*[35] *and MBEC Communications Inc. v. Nagel*[36], held that where there is clear breach of a restrictive covenant, the first element of the Three-part Test is satisfied and the additional elements of irreparable harm and balance of convenience need not be addressed.

In *Allegra II*, the court stated that while less emphasis should be placed on irreparable harm and balance of convenience in cases of clear breach of an express negative covenant, this "does not mean that there is no obligation to deal with these factors".[37] Similarly, in *Van Wagner Communications Co. v. Penex Metropolis Ltd.*, the court considered case law involving clear breach of restrictive covenants where irreparable harm and balance of convenience were considered, and cases where these two factors were ignored. The court held that "even where there is a clear breach of a negative covenant which is reasonable on its face, the issues of irreparable harm and balance of convenience cannot be ignored". However, these factors may be given less weight in determining the issue "depending on the strength of the plaintiff's case".[38] Although *Van Wagner Communications* is not a franchise law case, but rather dealt with a breach of an exclusive sales agency agreement for outdoor advertising, it is relevant as a recent affirmation that irreparable harm and balance of convenience will continue to be weighed by courts on interlocutory injunction motions.[39]

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[34] *Ibid.* at paras. 75 and 76.

[35] *Button v. Jones*, [2001] O.J. No. 1976 (Ont. Sup. Ct.).

[36] *MBEC Communications Inc. v. Nagel*, [2007] CarswellOnt 2042 (Ont. Sup. Ct.).

[37] *Allegra II, supra* note 29 at para. 30.

[38] *Van Wagner Communications Co. v. Penex Metropolis Ltd.*, [2008] O.J. No. 190 (Ont. Sup. Ct.) [*Van Wagner Communications Co.*] at para. 39.

[39] The decision of Justice Patillo in *Van Wagner Communications Co*., *supra*, was upheld on appeal by the Ontario Divisional Court (see *Van Wagner Communications Co. v. Penex Metropolis Ltd.*, [2008] O.J. No. 1707 (Ont. Sup. Ct. [Divisional Court]). Specifically, the Divisional Court affirmed that "Where a negative covenant is breached and a *prima facie* case is made out, regard must be had to irreparable harm and balance of convenience, but not to the same extent as where there is no negative covenant". The Divisional Court further held that it "cannot be said that there are conflicting decisions on the point in Ontario". However, an appellate court has yet to clarify the appropriate threshold test, as discussed above, and what constitutes irreparable harm on an interlocutory injunction.

Conclusion

Recent trends in the law of interlocutory injunctions in the franchise context suggest some practical implications of which franchisors should be aware. Previously, it was rare to be unsuccessful on an interlocutory injunction motion for failure to meet the first element of the Three-part Test, as courts simply applied the "serious issue to be tried" threshold. So long as a case was neither frivolous or vexatious, i.e. there was some possibility of success at trial, a plaintiff would satisfy the "serious issue to be tried" requirement. Now, when it's a matter of enforcing restrictive covenants, courts may be taking a harder look at the merits of the case itself at the interlocutory stage. As a result, when considering whether to pursue an interlocutory injunction, franchisors should consider the ultimate enforceability or strength of the restrictive covenant at issue, and whether the terms of the franchise agreement or termination agreement are unequivocal, before proceeding with an injunction.

Additionally, a franchisor who pursues an interlocutory injunction can no longer merely rely on persuasive arguments from prior cases with respect to compromised goodwill or general damage to the franchise system. Rather, the franchisor must be prepared to provide concrete evidence of actual irreparable harm suffered as a result of the breach of the restrictive covenant. If there are weaknesses on either of these fronts, a franchisor should tread cautiously when pursuing injunctive relief. Injunctions are costly and like all motions, if a moving party is unsuccessful, then not only must it pay its own lawyer's costs but it will be required to pay some of the responding party's costs. To avoid paying any of the franchisee's costs, the franchisor will have to try to settle with the franchisee by either offering to drop any appeal from the order of the court dismissing the injunction and/or to not pursue any action against the franchisee in respect of its alleged breach of the non-competition covenant.

To avoid the Three-part Test altogether, parties may wish to consider seeking injunctive relief by way of application instead of by motion.[40] That way, the Three-part Test does not apply since the injunction sought under an application is permanent (that is, until the covenant expires as opposed to until the trial is heard) and not interlocutory. Of course, the franchisor will still have to establish on a balance of probabilities that the covenant is enforceable and that it has been breached by the franchisee. The franchisor will also have to establish that damages are an inadequate remedy for any breach of the restrictive covenant and that franchisee's infringing conduct must therefore be enjoined.

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[40] Under Rule 14.05(3)(g) of the *Ontario Rules of Civil Procedure*, a proceeding may be brought by way of an application for an injunction, mandatory order . . . when ancillary to relief claimed in a proceeding properly commenced by a notice of application. In the case of an application to enforce a post-termination covenant, a franchisor should apply under Rule 14.05(3)(d) for a determination of rights that depend on the interpretation of a contract (in this case a franchise agreement) in addition to its application for an injunction to enforce the post-termination obligations under the franchise agreement. *W.A.B. Bakery Franchising*, *supra*, is an example of a franchisor commencing a proceeding to enforce a non-competition covenant by way of application. However, rather than seeking an injunction on a permanent basis, the franchisor sought an interlocutory injunction until the date of a decision by an arbitrator or the Court on the franchisor's request for a similar injunction on a permanent basis. As such, the Three-part Test applied. For the first part of the Three-part Test, the Court applied the serious issue to be tried test, even though what the Court was being asked to enforce was a restrictive covenant. In *Second Cup*, *supra*, the Court stated that the enforcement of a restrictive covenant required the higher standard of strong *prima facie* case.

Another option is for the franchisor at the commencement of the hearing of a motion for an injunction to ask for an expedited trial, well prior to the expiry of the restrictive covenant at issue. Obtaining an expedited trial date avoids the argument (raised in *Second Cup*, *supra* and *Lombardo*, *supra*) that the injunction will finally determine the matter. In the *Hyundai* case, *supra*, in which an interlocutory injunction was granted in favour of the franchisee on January 13, 2009, the Court ordered an expedited two-week trial to commence no later than April 30, 2009, only a little over three months away.[41]

Although the Ontario Divisional Court in *Van Wagner Communications*, *supra*, confirmed that all elements of the Three-part Test apply where there is a breach of a negative covenant, some uncertainty remains in the law of interlocutory injunctions in the franchise context. The apparent dichotomy between decisions in which courts have applied the thresholds of “serious issue to be tried” or “strong *prima facie case*”, as well as conflicting case law with respect to the evidentiary standard for proving irreparable harm suggest a need for clarification by an appellate court.

[41] There will not be en expedited trial, however, as the case has settled.